INDEX

	Page
Opinions below	1
Jurisdiction	1
Questions presented	2
Statute involved	2
Statement	2
Argument	5
Conclusion	12
Appendix	13

CITATIONS

Cases:	
Civil Aeronautics Board v. *Delta Lines, Inc.*, 367 U.S. 316	9, 10
J. H. Lederer Co., 38 S.E.C. 794	3
United States v. *Seatrain Lines, Inc.*, 329 U.S. 424	9, 10
Statute:	
Administrative Procedure Act, Section 8(b), 60 Stat. 242, 5 U.S.C. 1007(b)	7
Securities Exchange Act of 1934, 48 Stat. 881, as amended (15 U.S.C. 78a *et seq.*):	
Section 15A(b), as added, 52 Stat. 1070 (15 U.S.C. 78o–3(b))	3
Section 15(b)	2, 3, 5, 6, 7, 10, 13
Section 22	11

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In the Supreme Court of the United States

OCTOBER TERM, 1961

No. 585

N. SIMS ORGAN & CO., INC. AND N. SIMS ORGAN,
PETITIONERS

v.

SECURITIES AND EXCHANGE COMMISSION

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

BRIEF FOR THE SECURITIES AND EXCHANGE COMMISSION IN OPPOSITION

OPINIONS BELOW

The opinion of the Court of Appeals (Pet. App. A1–A8) is reported at 293 F. 2d 78. The findings and opinion of the Securities and Exchange Commission (Pet. App. B1–B12) are set forth in Securities Exchange Act Release No. 6495.

JURISDICTION

The judgment of the Court of Appeals affirming the order of the Securities and Exchange Commission was entered on September 19, 1961 (Pet. App. C1–C2).

The petition for a writ of certiorari was filed on December 4, 1961. The jurisdiction of this Court is invoked under Section 25(a) of the Securities Exchange Act of 1934, 15 U.S.C. 78y, and 28 U.S.C. 1254(1).

QUESTIONS PRESENTED

1. Whether, after a registration as a broker and dealer in securities had become effective by lapse of time before the merits of charges of fraudulent conduct were determined in a proceeding looking towards denial of registration, the Securities and Exchange Commission was precluded from considering the same charges in a proceeding to revoke the registration.

2. Whether publication in the Commission's daily news digest of notice that a proceeding has been instituted against an applicant for registration upon the basis of charges brought by the Commission's staff constitutes a prejudgment of the issues and a denial of due process.

STATUTE INVOLVED

The pertinent provisions of Section 15(b) of the Securities Exchange Act of 1934, 15 U.S.C. 780, 48 Stat. 895–896, as amended, 49 Stat. 1377–1378, are set forth in the Appendix, *infra*, pp. 13 to 16. The section is misquoted in the petition.

STATEMENT

The individual petitioner, N. Sims Organ, was a salesman employed by J. H. Lederer Co., Inc., a registered securities broker and dealer, during a period in 1958 in which that firm conducted a fraudulent

stock-selling campaign (Pet. App. B-8). These activities resulted in revocation of that company's registration on December 28, 1958 (Pet. App. B-3). See *J. H. Lederer Co.*, 38 S.E.C. 794. Within a month after the revocation, petitioner N. Sims Organ & Co. (referred to herein as Organ & Co.) was organized, and application was made thereafter for its registration as a broker and dealer (Pet. App. B-4). N. Sims Organ is the president, treasurer, a director and owner of ten percent or more of the stock of Organ & Co. (Pet. App. B-3).

Prior to the effective date of Organ & Co.'s registration the Commission instituted a proceeding under Section 15(b) of the Act to determine whether Mr. Organ, a controlling person of Organ & Co., had violated anti-fraud provisions of the federal securities acts when he had been employed by Lederer Co., and, if so, whether it was in the public interest to deny the application, and whether Mr. Organ was to be found the cause of any order of denial.[1] The order initiating the proceeding recited that members of the Commission's staff had reported information obtained as a result of an investigation which tended to show the violations charged (R. 16a). In the same order, and again pursuant to Section 15(b), the Commission postponed the effective date of Organ & Co.'s registration for 15 days until December 21, 1959, and directed that a preliminary hearing before one of its

[1] Pursuant to Section 15A(b)(4) of the Act, as added, 52 Stat. 1070, such a finding renders it difficult for an individual to engage in the securities business.

hearing examiners be held to determine whether the effective date of registration should be further postponed pending the denial proceedings (R. 18a). The order also stated that, if the effective date were postponed, a further hearing would be held on the question of denial of registration (R. 13a).

The preliminary hearing was conducted December 2, 1959, and the examiner transmitted the hearing record to the Commission without filing a recommended decision. Thereafter, no further action was taken by the Commission, its staff or the examiner until January 28, 1960 (R. 18a). No determination was made whether the evidence adduced at the hearing warranted a further postponement of the date of registration while the merits of the charges of fraudulent activities were to be heard and decided.

As a result of the lapse of time, Organ & Co.'s registration became effective on December 21, 1959 (R. 20a). Thereafter, on January 28, 1960, the Commission ordered the denial proceeding dismissed on the ground that it had become moot and instituted a proceeding on the same charges to revoke the registration, which resulted in the order now under review (R. 19a–22a). At the ensuing hearing before the same examiner, the record developed in the preliminary hearing on postponement was included by consent as part of the record. Some additional evidence was received, although none of the evidence pertained to activities subsequent to the effective date of Organ & Co.'s registration (R. 23a; 54a–58a).

As appears from the Commission's detailed findings and opinion (Pet. App. B1–B12), the Commis-

sion found that Mr. Organ, in willful violation of anti-fraud provisions of the Securities Act and the Securities Exchange Act, had made misrepresentations over the long-distance telephone while employed by Lederer Co.[1] In view of these willful violations, the Commission concluded that it was in the public interest to revoke Organ & Co.'s registration. The Commission entered an order of revocation and found that Mr. Organ was a cause of such revocation (Pet. App. B13–14).

The Court of Appeals for the Second Circuit affirmed this order, agreeing with the Commission that the evidence established that Mr. Organ had made the misrepresentations charged (Pet. App. A5). The court also considered and rejected other contentions by petitioners which are repeated in the instant petition (Pet. App. A6–A8).

ARGUMENT

The decision of the court below was correct and does not conflict with the decisions of this Court or of other courts of appeals.

1. Petitioners apparently contend that the Commission is without authority under Section 15(b) of the Securities Exchange Act of 1934 to revoke the registration of a broker and dealer in securities where the evidence of violations upon which a revocation could otherwise be based may have been known to the Commission or its staff prior to the date the

[1] In this regard the Commission differed from the examiner who had found the evidence insufficient to tie the individual petitioner to the fraudulent activities.

application for registration became effective. Relying on the abortive proceeding to determine whether to postpone the registration, they argue that the doctrine of *res judicata* buttresses their contention.[3] The governing statute, however, as the court below held, does not compel the anomalous result sought, whereby a person who is found on a proper record to have willfully violated anti-fraud provisions of the federal securities laws must be permitted to remain in the securities business, contrary to the public interest, merely because proceedings might have been brought against him at a somewhat earlier date.

Section 15(b) of the Securities Exchange Act provides that "the Commission shall, after appropriate notice and opportunity for hearing, by order deny registration to or revoke the registration of any broker or dealer if it finds that such denial or revocation is in the public interest" and, *inter alia,* that the controlling person of the broker or dealer has willfully violated anti-fraud provisions of the statute or of the Securities Act of 1933. The grounds for denial and revocation are the same, and it is expressly provided that either sanction may be based on misconduct committed by the controlling person, "whether prior or subsequent to" his affiliation with the particular broker or dealer.

In the absence of institution of proceedings by the Commission, an application for registration under

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[3] Petitioners nowhere claim that they changed position to their detriment following the effective date of the registration and prior to the institution of revocation proceedings five weeks later.

Section 15(b) of the Act becomes automatically effective thirty days after filing. Where the Commission initiates a proceeding to determine whether to deny an application, Section 15(b) specifically empowers it, without a hearing, to postpone the effective date of registration for a period not exceeding fifteen days. In addition, the Commission is authorized to postpone the effective date for an indefinite period pending final determination of the denial proceeding where, after notice and opportunity for hearing, such postponement "shall appear to the Commission to be necessary or appropriate in the public interest or for the protection of investors."[4]

There is nothing in the statute, its legislative history or in the petition which indicates that Congress intended that the Commission's failure to institute denial proceedings prior to the effective date of a registration application would grant the applicant immunity from a subsequent revocation based upon any information then known to the Commission or its staff. The statute is remedial in nature and is to be interpreted in accordance with its purpose, which is to protect the public from brokers, dealers,

[4] It is and has uniformly been the Commission's administrative practice to issue an order upon termination of any hearing proceeding. This, in fact, is a requirement of Section 8(b) of the Administrative Procedure Act (5 U.S.C. 1007(b)). No such order was issued here prior to the date registration was to become effective or thereafter until January 28, 1960, when revocation proceedings were instituted. Thus, Mr. Organ, who was not a newcomer to the securities business and who was represented by counsel in the proceedings, should have recognized that review of the charges had not been concluded.

and other persons who have engaged in activities violating the securities legislation. In effect, the abortive denial proceeding was rendered a nullity by the Commission's failure to act. Thus, it should be given no greater legal effect than is given the Commission's failure initially to set down for hearing an application as to which there was in its files some evidence of misconduct.

In petitioners' case, since the Commission had not determined whether the public interest warranted a further postponement, the registration became effective without review or decision of the merits of any of the charges. By initiating the revocation proceeding upon the identical charges shortly thereafter,[5] the Commission, in essence, continued the proceeding, so that the merits of the outstanding and undermined charges could be decided. Since Section 15(b) sets forth identical grounds for denial and revocation, it necessarily contemplates that revocation might be premised on violations prior to registration.

As pointed out by the Court of Appeals (Pet. App. A7–A8), since nothing was decided in either the preliminary hearing on postponement or the denial proceeding that had become moot, *res judicata* is clearly

[5] Registration became effective on December 21, 1959. The order dismissing the denial proceeding as moot and instituting the revocation proceeding was entered on January 28, 1960 (see, *supra*, at pp. 3–4).

inapplicable. Although petitioners concede that no determination was made by the Commission (Pet. 6), they nonetheless claim effects of *res judicata* for its inaction. However, the cases cited at page 12 of their petition are not in point. Each involved a situation where a determination, either explicit or implicit, had been made in some prior proceeding. Here the Commission failed to act at all. No explicit determination was made. No implicit determination can be spelled out from its lack of action in the denial proceeding prior to the time the registration became effective. Nor is the situation in this case in any way comparable to the hypothetical situation set forth at page 13 of the petition where "a lawyer could be disbarred for matters that had been thoroughly aired by the Character Committee before his admission." Presumably the character committee is required to make a determination prior to admission; the Commission is not required by the statute to make a determination prior to effectiveness of a registration.

The decision below is not in conflict with *Civil Aeronautics Board* v. *Delta Lines, Inc.*, 367 U.S. 316,* or *United States* v. *Seatrain Lines, Inc.*, 329 U.S.

* Petitioners inappropriately insert "[SEC]" in quoted material from the opinion of this Court in *Civil Aeronautics Board* v. *Delta Lines, Inc.*, appearing at page 10 of the petition. The Commission was not involved in that action in any respect.

494, as petitioners contend (Pet. 9). Revocation here occurred after petitioners had the full evidentiary hearing contemplated by the Securities Exchange Act, whereas in *Delta Lines, Inc.*, this Court rested its holding on the fact that the respondent had not been afforded the hearing required by the Federal Aviation Act. Moreover, the certificate of public convenience and necessity there involved had been granted by a decision of the Civil Aeronautics Board after a hearing and cannot be equated with an application for registration under Section 15(b) of the Securities Exchange Act which became effective automatically after filing without any action on the part of the Commission. In *United States* v. *Seatrain Lines, supra*, it was held that the statute, the Interstate Commerce Act, did not authorize revocation of the certificate held by respondent. Section 15(b) of the Securities Exchange Act, however, as we have seen, specifically authorizes revocation.

2. The Court of Appeals correctly rejected petitioners' charge that the notice of the administrative proceedings in the Commission's daily news digest constituted prejudgment of the issues or was otherwise violative of due process (Pet. App. A6–A7). While the court believed that the wording created "an impression which could be interpreted as tending to indicate that the Commission had already made up its mind" (Pet. App. A7), it pointed out that it did not believe such impression was intended.

The item in question was entitled "FRAUD CHARGED TO N. SIMS ORGAN CO." and recited:

> The SEC has issued an order under the Securities Exchange Act of 1934 postponing the effective date of registration of N. Sims Organ & Co., Inc., 460 E. Park St., *Long Beach, L.I., New York,* as a broker-dealer, and ordering a hearing on the question whether such registration should be denied. B. [*sic*] N. Sims Organ is president, treasurer, director, and owner of 10% or more of the common stock of N. Sims Organ & Co., Inc.

It then set forth that:

> The order of the Commission asserts that members of its staff have reported information obtained as a result of an investigation which tends to show that * * *

the anti-fraud provisions of the federal securities acts had been violated by Mr. Organ in the manner described therein.

Pursuant to statute it is the Commission's function to institute disciplinary proceedings based upon information reported to it by its staff. Section 22 of the Securities Exchange Act, 15 U.S.C. 78v, which provides that hearings under the Act "may be public," is authorization to the Commission to alert the investing public, where, as here, a salesman with whom they may be dealing has been charged with willful violations of the anti-fraud provisions of the federal securities acts. Such releases reporting the

results of staff investigations are customarily issued in the performance of this statutory duty and do not prejudice the Commission's subsequent consideration of the charges.'

CONCLUSION

For the foregoing reasons, the petition for a writ of certiorari should be denied.

Respectfully submitted.

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General Counsel,
DAVID FERBER,
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Attorney,
Securities and Exchange Commission.

JANUARY 1962.

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[1] In deference to the attitude of the court below the Commission now phrases releases giving notice of the institution of revocation or denial proceedings in terms which make explicit that it is acting upon the recommendation of the staff, which, as the complainant, has reason to believe that violations have occurred. See, for example, Securities Exchange Act Release Nos. 6666 (November 3, 1961) and 6690 (December 20, 1961).

APPENDIX

SECURITIES EXCHANGE ACT OF 1934

OVER-THE-COUNTER MARKETS

SECTION 15. (b) A broker or dealer may be registered for the purposes of this section by filing with the Commission an application for registration, which shall contain such information in such detail as to such broker or dealer and any person directly or indirectly controlling or controlled by, or under direct or indirect common control with, such broker or dealer, as the Commission may by rules and regulations require as necessary or appropriate in the public interest or for the protection of investors. Except as hereinafter provided, such registration shall become effective thirty days after the receipt of such application by the Commission or within such shorter period of time as the Commission may determine.

An application for registration of a broker or dealer to be formed or organized may be made by a broker or dealer to which the broker or dealer to be formed or organized is to be the successor. Such application shall contain such information in such detail as to the applicant and as to the successor and any person directly or indirectly controlling or controlled by, or under direct or indirect common control with, the applicant or the successor, as the Commission may by rules and regulations require as necessary or appropriate in the public interest or for the protection of investors. Except as hereinafter provided, such regis-

tration shall become effective thirty days after the receipt of such application by the Commission or within such shorter period of time as the Commission may determine. Such registration shall terminate on the forty-fifth day after the effective date thereof, unless prior thereto the successor shall, in accordance with such rules and regulations as the Commission may prescribe, adopt such application as its own.

If any amendment to any application for registration pursuant to this subsection is filed prior to the effective date thereof, such amendment shall be deemed to have been filed simultaneously with and as part of such application; except that the Commission may, if it appears necessary or appropriate in the public interest or for the protection of investors, defer the effective date of any such registration as thus amended until the thirtieth day after the filing of such amendment.

The Commission shall, after appropriate notice and opportunity for hearing, by order deny registration to or revoke the registration of any broker or dealer if it finds that such denial or revocation is in the public interest and that (1) such broker or dealer whether prior or subsequent to becoming such, or (2) any partner, officer, director, or branch manager of such broker or dealer (or any person occupying a similar status or performing similar functions), or any person directly or indirectly controlling or controlled by such broker or dealer, whether prior or subsequent to becoming such, (A) has willfully made or caused to be made in any application for registration pursuant to this subsection or in any document supplemental thereto or in any proceeding before the Commission with respect to registration pursuant to this subsection any statement which was at the time

and in the light of the circumstances under which it was made false or misleading with respect to any material fact; or (B) has been convicted within ten years preceding the filing of any such application or at any time thereafter of any felony or misdemeanor involving the purchase or sale of any security or arising out of the conduct of the business of a broker or dealer; or (C) is permanently or temporarily enjoined by order, judgment, or decree of any court of competent jurisdiction from engaging in or continuing any conduct or practice in connection with the purchase or sale of any security; or (D) has wilfully violated any provision of the Securities Act of 1933, as amended, or of this title, or of any rule or regulation thereunder. Pending final determination whether any such registration shall be denied, the Commission may by order postpone the effective date of such registration for a period not to exceed fifteen days, but if, after appropriate notice and opportunity for hearing, it shall appear to the Commission to be necessary or appropriate in the public interest or for the protection of investors to postpone the effective date of such registration until final determination, the Commission shall so order. Pending final determination whether any such registration shall be revoked, the Commission shall by order suspend such registration if, after appropriate notice and opportunity for hearing, such suspension shall appear to the Commission to be necessary or appropriate in the public interest or for the protection of investors. Any registered broker or dealer may, upon such terms and conditions as the Commission may deem necessary in the public interest or for the protection of investors, withdraw from registration by filing a written notice of withdrawal

with the Commission. If the Commission finds that any registered broker or dealer, or any broker or dealer for whom an application for registration is pending, is no longer in existence or has ceased to do business as a broker or dealer, the Commission shall by order cancel the registration or application of such broker or dealer.

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U.S. GOVERNMENT PRINTING OFFICE: 1963